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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

Nos. 510-511.

ESTATE OF CORDELIA Y. ABENDROTH, CITY BANK FARMERS TRUST COMPANY, as Executor of the Last Will and Testament of Cordelia Y. Abendroth, deceased,

Petitioner,

—against—

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ESTATE OF KATE READ BLACQUE, CITY BANK FARMERS TRUST COMPANY, as Executor of the Last Will and Testament of Kate Read Blacque, deceased,

Petitioner,

—against—

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR PETITIONERS.

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BRIEF FOR PETITIONERS.

Opinions Below.

The majority opinion (R. 86) and the dissenting opinion (R. 87) of the Board of Tax Appeals are reported in 41 B. T. A. 1178. The *per curiam* opinion of the Circuit Court of Appeals (R. 113) is reported in 114 F. (2d) 1017.

Jurisdiction.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925. The judgments of the Circuit Court of Appeals were entered October 10, 1940 (R. 114, 116). The petition for writs of certiorari was filed October 16, 1940, and granted November 18, 1940.

Question Presented.

Where an executor elects to exercise the option provided in Section 302(j) of the Revenue Act of 1926, as added by Section 202 of the Revenue Act of 1935, to report the assets of the estate in the Federal estate tax return at their values one year after the decedent's death, must there be included in the gross estate, in addition to the property owned by the decedent at the date of death, ordinary dividends and bond interest accruing between the date of death and such optional valuation date?

The Statute.

The statute involved is Title III of the Revenue Act of 1926, as amended, and more particularly the following sections:

> "Sec. 301. (a) In lieu of the tax imposed by Title III of the Revenue Act of 1924, a tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 303) is hereby imposed upon the transfer of the net estate of every decedent dying after the enactment of this act, whether a resi-

dent or nonresident of the United States; [then follow the tax rates].

"Sec. 302. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated * * *"

"(j) [as added by Sec. 202(a) of the Revenue Act of 1935] If the executor so elects upon his return (if filed within the time prescribed by law or prescribed by the Commissioner in pursuance of law), the value of the gross estate shall be determined by valuing all the property included therein on the date of the decedent's death as of the date one year after the decedent's death, except that (1) property included in the gross estate on the date of death and, within one year after the decedent's death, distributed by the executor (or, in the case of property included in the gross estate under subdivision (c), (d), or (f) of this section, distributed by the trustee under the instrument of transfer), or sold, exchanged or otherwise disposed of, shall be included at its value as of the time of such distribution, sale, exchange, or other disposition, whichever first occurs, instead of its value as of the date one year after the decedent's death, and (2) any interest or estate which is affected by mere lapse of time shall be included at its value as of the time of death (instead of the later date) with adjustment for any difference in its value as of the later date not due to mere lapse of time. No deduction under this title, of any item shall be allowed if allowance for such item is in effect given by the valuation under this subdivision. Wherever in any other subdivision or section of this title or in Title II of the Rev-

enue Act of 1932, reference is made to the value of property at the time of the decedent's death, such reference shall be deemed to refer to the value of such property used in determining the value of the gross estate. In case of an election made by the executor under this subdivision, then for the purposes of the deduction under section 303(a)(3) or section 303(b)(3), any bequest, legacy, devise, or transfer enumerated therein shall be valued as of the date of decedent's death with adjustment for any difference in value (not due to mere lapse of time or the occurrence or nonoccurrence of a contingency) of the property as of the date one year after the decedent's death (substituting the date of sale or exchange in the case of property sold or exchanged during such one-year period)."

The Regulation.

The regulation here in issue is Article 11 of Regulations 80 (1937 edition), the pertinent parts of which are set forth in an appendix, *infra*, pages 45-49.

The Facts.

All the facts were stipulated and are set forth in two stipulations, one applicable to each estate (R. 29, 48).

Cordelia Y. Abendroth died on October 9, 1936, and Kate Read Blacque died on April 3, 1937 (R. 29, 48). The executor in each case elected upon the return to have the gross estate valued as of one year after death, or, as to property disposed of during such one-year period, as of the date of such disposition, as permitted by Section 302(j) (R. 30, 49).

After Mrs. Abendroth's death, her estate collected $1,793.26 of interest which accrued within one year after the date of her death on bonds owned by her at the date of her death, and $1,990.65 of ordinary dividends declared and payable on corporate stocks owned by her at the date of her death, out of earnings of the paying corporations, to stockholders of record as of various dates within one year after her death (R. 32). Income of $3,783.91 was thus earned during the period of one year after death on the assets owned on the date of death.

After Mrs. Blacque's death, her estate collected $6,653.87 of interest which accrued within one year after the date of her death on bonds earned by her at the date of her death, and $47,210.58 of ordinary dividends declared and payable on corporate stocks owned by her at the date of her death, out of earnings of the paying corporations, to stockholders of record as of various dates within one year after her death (R. 51). Income of $53,864.45 was thus earned during the period of one year after death on the assets owned on the date of death.

The return in each case included in the gross estate all bond interest accrued to the date of death but payable thereafter, and all dividends which were declared and payable after death to stockholders of record as of a date prior to death (R. 31, 50). Those items of income accrued prior to death are not in dispute.

The executor in each case omitted from the gross estate the items of income accrued after death, but the Commissioner added such items to the gross estate (R. 32-33, 51-52).

For example, Mrs. Abendroth owned 45 shares of American Telephone and Telegraph Company, stock

At the time of her death this stock carried a right to a dividend theretofore declared which was payable after her death to stockholders of record prior to her death, in the amount of $101.25. The executor included that dividend in the estate tax return as a separate item (in addition to the value of the stock itself, "ex-dividend") and it is not in dispute. In addition to that dividend, the Commissioner has added to the gross estate three dividends of $101.25 each paid within one year after death to stockholders of record as of a date within such one year period, and one dividend of $101.25 paid more than one year after death to stockholders of record as of a date within one year after death. In this way, the Commissioner has increased the gross estate by the amount of four regular quarterly dividends received after the decedent's death, in addition to the one dividend which the executor included in the estate because it was payable to stockholders of record as of a date prior to death (R. 34).

Mrs. Abendroth also owned $2,000 principal amount of Central Pacific Railway 5% Bonds, on which interest of $19.17 had accrued to October 9, 1936, the date of death. The executor included this item of accrued interest in the estate tax return as a separate item (in addition to the value of the bond, exclusive of interest) and it is not in dispute. In addition to the interest accrued to the date of death, the Commissioner has added to the gross estate the semi-annual instalment of interest paid February 1, 1937 ($50), less the amount thereof which had accrued to the date of death, a net amount of $30.83; the full semi-annual instalment of interest paid August 1, 1937, in the amount of $50; and the interest accrued from August 1, 1937 through October 9,

1937 (one year after death) in the amount of $19.17. In this way, the Commissioner increased the gross estate by one full year's interest on such bonds (R. 36).

It is not entirely clear from Exhibit A annexed to each Stipulation of Facts that the Commissioner included in the gross estate one full year's bond interest in addition to the interest accrued to the date of death. However, paragraphs 7 and 8 of the Stipulation of Facts in each case show that that is what the Commissioner did (R. 31-32; 50-51).

The estate tax deficiencies here in dispute ($432.83 in the *Aboudroth* case and $13,996.28 in the *Blacque* case) were due entirely to the Commissioner's addition to the gross estate of the items of interest and dividends accrued after death as hereinabove set forth.

The Rulings Below.

The Board of Tax Appeals affirmed the Commissioner's determination on the authority of the decision of the court below in *Maass* v. *Higgins* (*sub nom. Saks* v. *Higgins*, 111 F. (2d) 78), now pending in this Court on writ of certiorari, No. 274, October Term, 1940. There was a dissenting opinion by four members of the Board.

The court below affirmed the Board, *per curiam*, on the authority of its decision in *Maass* v. *Higgins*.

Specification of Errors.

The Circuit Court of Appeals erred, in each case:

1. In holding that Section 302(j) of the Revenue Act of 1926, as amended, requires the inclusion in

the decedent's gross estate of the interest and dividends accruing after death upon bonds and stocks owned by the decedent at the date of death, and in failing and refusing to hold that such interest and dividends should be excluded from the gross estate.

2. In holding that said interest and dividends constituted a part of the property owned by the decedent at the date of death.

3. In upholding the validity of the regulations of the Treasury Department requiring the inclusion of such interest and dividends in the gross estate.

4. In affirming the decision of the Board of Tax Appeals.

Summary of Argument.

Irrespective of whether or not the optional valuation privilege is availed of, the same provisions of the estate tax law impose the tax on the decedent's estate which is transferred by reason of his death, and define such estate as comprising all property "to the extent of the interest of the decedent therein at the time of his death", with certain additions not here material, including property transferred by him in contemplation of or intended to take effect at or after his death.

In the usual case, such property is valued as of the date of death, and it is perfectly well settled that, in such case, income earned after death is not to be included therein.

If the option granted by Section 302(j) is exercised, the same property is to be valued as of one year after the decedent's death. No mention is made of income after death.

So far as the language of the statute is concerned, there is no more ground for treating the income after death as a part of the estate in one case than in the other.

The income after death was not in existence at the date of death and was not, in fact, a part of the decedent's estate at that time.

It follows necessarily from previous decisions of this Court that such income may not be treated as constituting, in theory, a part of the decedent's estate at the time of his death.

Unless the income after death actually depleted the assets in the estate at the date of death and therefore reduced their value, there is no reason for treating such income, contrary to fact, as if it were a part of the decedent's estate at the time of his death.

The interest and dividends received after death by the estates in these cases did not deplete the bonds and stocks on which they were earned, or reduce their value. The interest was the usual kind of bond interest and the dividends were ordinary dividends paid in the regular course of business. This Court has held that such interest and dividends are income and, for that very reason, may not be treated, to any extent, as a return of capital.

The statute is unambiguous, but if interpretation be required, the legislative history shows that Con-

gress intended that income after death should not be added to the estate if the optional valuation were used.

It is not necessary, as the Treasury contends, to include in the estate the income after death, in order to prevent tax evasion.

In any event, the Treasury's "interpretation" of the statute should be disapproved; it would treat ordinary dividends and interest as constituting, at one and the same time, both capital and income to the estate and thus would impose an unjust burden of double taxation which there is no reason to believe Congress would approve.

Argument.

The petitioners' case might well be rested on the dissenting opinion of Judge Chase in *Maass* v. *Higgins* and the opinion of Judge Chesnut (D. C. Md.) in *Clark* v. *United States*, 33 F. Supp. 216. Those opinions are so convincing and comprehensive that nothing in the way of argument need be added and, indeed, little can be added.

Necessarily, this brief will be found to contain many of the points which have been developed fully in those opinions. We shall, however, present certain additional considerations which we believe will further fortify the conclusion reached by Judge Chase and Judge Chesnut.

I.

The express language of the statute excludes from the estate any property, whether capital or income, not a part of the decedent's estate on the date of his death.

It clearly was within the power of Congress to require the estate tax to be computed on the basis of the capital assets owned at the date of death plus the income produced during the year after death, as the price of exercising the option of valuing the assets of the estate as of one year after death.

The question here is whether Congress has done so.

The first thing to be observed is that the statute contains no reference to income after death, but provides specifically that, irrespective of whether the assets of the estate be valued as of the date of death or as of one year later, the tax shall be computed on the property in the decedent's estate at the date of his death. Congress has said, as plainly as it could, that in either event the tax is laid on the same assets, with only a change in their valuation.

What property is to be considered as within the decedent's estate at the date of his death may, indeed must, be ascertained by an examination of the estate tax law in effect before the enactment of the optional valuation provision, and the rulings and decisions interpreting it.

Section 301 imposes the estate tax "upon the transfer of the net estate of every decedent". Section 303 defines the net estate as "the gross estate" less certain exemptions and deductions.

Section 302 provides that the value of the decedent

ent's gross estate shall be determined "by including the value at the time of his death of all property * * * (a) *to the extent of the interest therein of the decedent at the time of his death*" plus property transferred by the decedent during his life in certain specified ways, property over which he has exercised a general power of appointment and proceeds of insurance taken out by the decedent on his own life.

Although the estate tax return is not required to be filed until fifteen months (formerly one year) after death and although deductions are specifically allowed in computing the tax for all administration expenses during that period (Sec. 303(a)(1)), it always has been well settled that no account need be taken of any income earned by the estate during administration or at any time after the decedent's death.[1]

In the administration of the law no effort ever has been made to impose the tax on income earned after death, except in one case where it was obvious that the Treasury, being uncertain as to whether a particular item represented a part of the estate's capital at the date of death or income earned thereafter, taxed it as both. *Bull* v. *United States*, 295 U. S. 247. In that case, this Court determined that the item represented income earned after death and therefore was not subject to estate tax as a part of the decedent's estate.

In the administration of two special provisions of the law prior to the enactment of the optional valuation provision, the Treasury was called upon to deter-

[1] Income taxes on income after death and property taxes accruing after death are excluded from the allowable administrative expenses by Sec. 303(a)(1).

mine whether the problem of valuing as of a later date capital assets in existence on an earlier date required the inclusion of the income earned in the intervening period. In neither instance did the Treasury require the inclusion of such income.

Section 303(a)(2) of the estate tax law provides that, subject to certain limitations, a deduction shall be allowed for an amount equal to the value of "any property" acquired by the decedent from a person who died within five years prior to the decedent's death and in whose estate the property was subjected to estate tax. The deduction is limited to the value on the date of the first decedent's death or the value on the date of the second decedent's death, whichever is lower. The regulations (Art. 41, Reg. 80) do not provide that, where the property in the first decedent's estate is valued as of the date of the second decedent's death, the income in the intervening period shall be included, and, so far as we have been able to ascertain, no contention that it should be included ever has been advanced by anyone.

Section 302(c) provides for the inclusion in the decedent's gross estate of the value, as of the date of his death, of the decedent's interest in any property which he transferred during his life in contemplation of death or to take effect at or after his death. Here again, in valuing as of the date of the decedent's death property transferred by the decedent before his death, the Treasury never has attempted to include the income of the intervening period.

The question whether the income after death forms a part of the estate which was transferred by reason of death is involved also in other general provisions

of the estate tax law. Section 315(a) provides that the estate tax "shall be a lien for ten years upon the gross estate of the decedent". The Surrogate's Court of Westchester County, New York, has held that this lien "attaches only to the corpus and not to the income produced after death". The Surrogate said that "by no stretch of the imagination can it be said that the lien attaches to anything more than the estate existing at the date of death", and added, *ad passim*, that "Inasmuch as estate taxes are levied as of the date of death, income thereafter produced may not be considered in computing the taxable estate." *Matter of Andrus*, 169 Misc. (N. Y.) 740.

Section 315(b) provides that the lien for the tax shall attach also to any property transferred by the decedent during his life in such a way as to be subject to estate tax, "to the extent of the decedent's interest therein at the time of such transfer". So far as we have been able to ascertain, it never has been contended that the lien of the tax attaches to the income which was received, and probably spent, by the transferee after the transfer.

The particular provision here in question, Section 302(j), was enacted as an integral part of the statutory scheme just described. It provides that, at the option of the executor "the value of *the gross estate* shall be determined by valuing all the property *included therein on the date of the decedent's death*" at its value one year after death, or as to property disposed of during the one year period, at its value on the date of such disposition.

Section 301, which imposes the tax upon the transfer of the decedent's estate, remains applicable as in the ordinary case, as do the other provisions of Sec-

tion 302, which prescribe what property shall be included in the gross estate.

The "*gross estate*" which is to be valued as of one year after death is the same "*gross estate*" which was in existence and capable of ascertainment and valuation on the date of the decedent's death. It is *the decedent's* estate. It consists of the property *owned by the decedent at his death;* with certain additions not here material, which passes by reason of his death. No part of that property may be omitted from the optional valuation, even if it since has been sold, distributed, consumed or otherwise disposed of, and nothing else need be added.

It is conceded that if an asset of the decedent has been exchanged for another asset, it is the value of the original asset which must be included (as of the date of the exchange) and not the value of the new asset as of one year after death, no matter how much more or how much less it then may be worth. If a bond, worth $1,000 at death, is exchanged six months later, when it is worth $500, for another bond of equal value, the original bond is included in the estate at the value of $500 and the new bond is ignored, irrespective of what its value may be one year after death.

Only changes in value of the property existing at the date of death are to be taken into account. Changes in the property itself are to be ignored. All the assets of "the gross estate", "all the property included therein on the date of the decedent's death" must be valued as of one year after death or, if disposed of sooner, as of the date of disposition.

As to property which is wholly or partially destroyed by fire or other casualty during the one-year

period, the resulting loss (adjusted for any insurance received) is taken into account whether or not the optional valuation method is used. Section 303(a)(1) allows the deduction from the gross estate of any loss during the period of administration caused by fire, storm, shipwreck or other casualty, or by theft, to the extent not compensated for by insurance, provided the estate does not claim an income tax deduction for such loss.[2]

These results flow from the express direction of the statute to determine the *gross estate of the decedent* by valuing "*all the property included therein on the date of the decedent's death*" as of one year after death or, as to property theretofore disposed of, as of the date of disposition.

If Congress intended to make an exception to this general statutory scheme, so as to require the addition to the decedent's gross estate at the time of his death of the income earned by the estate during the one year after his death, which income did not exist at the date of his death and might never come into existence, it would have been a simple matter to say so in language which could not be misunderstood. The fact that Congress did not say so should be sufficient proof that it had no such intention (*United States* v. *Field*, 255 U. S. 257, 264), especially since, as we shall show, such a requirement would run counter to established principles long embedded in the estate tax law.

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[2] In order to make certain that a double estate tax benefit for such a loss shall not be allowed in case the optional valuation method is used, Sec. 302(j) provides that "no deduction under this title of any item shall be allowed if allowance for such item is in effect given by the valuation under this subdivision".

We show below that in enacting the optional valuation provision Congress in fact did not intend to subject the income after death to the estate tax. But, even if Congress had had such an intention, it could not be given effect, because nowhere in the statute is there any "language which can be reasonably construed to effect it". *Smietanka* v. *First Trust and Savings Bank*, 257 U. S. 602, 606.

The income after death is subject to income tax against the estate. To subject it also to estate tax would result in a duplication of taxes which, as this Court has said, "even in an exigent war tax measure is to be avoided unless required by express words". *United States* v. *Supplee-Biddle Hardware Co.*, 265 U. S. 189, 196. In a large estate the two taxes in the aggregate would exceed the income itself.

If there were any doubt as to the meaning of the provision, such doubt should be resolved against the claimed tax (*Shwab* v. *Doyle*, 258 U. S. 529, 536).

The provision was intended to afford relief from taxation and therefore should be liberally construed and applied. *Helvering* v. *Bliss*, 293 U. S. 144, 150-151.

II.

Income earned after death is not, in fact, part of the decedent's estate at the time of his death.

The Treasury concedes that the statute imposes the alternative optional tax only on the property in the estate at the date of death. It does not assert that the income earned after death was in existence at the date of death. But the Treasury seeks to solve the dilemma in which it finds itself by advancing the theory that every capital asset owned at the date of

death included the "right" to all future income to be derived therefrom, and that the subsequent receipt of the income thus represents a partial realization of the capital asset.

It is said that a bond comprises a "right" to repayment of the principal amount and a "right" to receive interest at the fixed rate until maturity. It is said that corporate stock includes a "right" to receive future dividends, when, as and if declared, out of the existing surplus of the corporation and any earnings that may be made in the future; and that real property includes a "right" to receive rent for its future use.

The highly intricate and artificial theory thus advanced by the Treasury finds no support in fact or in law.

On the date of the decedent's death, there was no existing property right in the so-called future income from his capital. That is so because such "future income" was not then in existence, but was only "an expectancy of income, or income, more accurately, in the process of becoming." *United States* v. *Safety Car Heating Company*, 297 U. S. 88, 99.

In the case of an interest-bearing bond, the decedent did have a contract right to receive interest when and as it should accrue, but that right ripened into an existing property right only when and as interest actually accrued through lapse of time.

As to rent accruing after death on an existing lease on real property, it is well established that rent grows out of the land and is paid for the right of occupancy; rent is not apportionable but accrues on the dates fixed for its payment. Until rent day, there is no existing obligation to pay or right to receive rent.

In re Roth and Appel, 181 Fed. 667, C. C. A. (2); *Manhattan Properties, Inc.* v. *Irving Trust Company*, 291 U. S. 320.

As to real property vacant at the date of death, there is at that time not even a conditional or inchoate right to any "future rent".

As to any dividends not already declared on corporate stock, the decedent had only a hope.

The Treasury Regulation is nothing but a thinly disguised assertion that the income arising after death is itself a part of the property owned at death. The assertion not only is contrary to fact but also ignores the fundamental distinction between capital and income.

In *Eisner* v. *Macomber*, 252 U. S. 189, this Court said, at page 206:

> "The fundamental relation of 'capital' to 'income' has been much discussed by economists, the former being likened to the tree or the land, the latter to the fruit or the crop; the former depicted as a reservoir supplied from springs, the latter as the outlet stream to be measured by its flow during a period of time."

In the same case, this Court said (p. 207) that income from property is

> "not a *growth* or *increment* of value *in* the investment; but a gain, a profit, something of exchangeable value *proceeding from* the property, *severed from* the capital however invested or employed, and *coming in*, being '*derived*', that is, *received* or *drawn by* the recipient (the taxpayer) for his *separate* use, benefit and disposal." (Italics the Court's.)

Since income from property is something "derived from capital" "proceeding from the property" and "severed from the capital", it cannot be said that such income is merely a part of the capital or property itself.

If on the date of his death the decedent owned land on which no crops were planted and one year after his death the land was in exactly the same condition, but in the meantime a crop had been planted and had matured and been harvested, it would be impossible to say that the crop was a part of the land at the time of the decedent's death.

If the decedent left vacant real property and, during the one year period after his death the executor leased such property and received rent therefrom, it simply would be contrary to fact to say that the rent was a part of the property owned by the decedent at the time of his death. The situation would be no different even if the property had been leased by the decedent prior to his death; the rent paid for the use of the property after the decedent's death would not represent an interest in the property at the time of his death.

Interest accrued to the date of death is subject to income tax imposed on the decedent with respect to his income up to the date of his death, but it is capital *to his estate* and, when subsequently received by the estate, is not income of the estate and is not subject to income tax. *Nichols* v. *United States*, 64 Ct. of Cls. 241, cer. den. 277 U. S. 584. Similarly as to dividends and other income.

This Court has held squarely in two cases that income earned by a decedent's estate after his death is not a part of his estate which was transferred to his heirs by reason of his death.

In *Bull* v. *United States, supra,* the estate of a deceased member of a partnership was entitled for a period of one year after his death "to receive the same interests, or participate in the losses to the same extent" as the deceased partner would, if living. The question was whether the amount received by the estate as its share of the partnership income during the one-year period was subject to estate tax or to income tax, or to both. This Court held that the amount so received by the estate was subject to income tax as income but was not subject to estate tax. The Court said, in effect, that the right of the deceased partner to participate in the firm earnings after his death was not a capital asset of his and therefore it did not become a capital asset of his estate upon his death, and thus was not subject to estate tax; but that, not being a part of the estate's original capital, it was income to the estate and therefore subject to income tax.

The question also came before this Court in *Irwin* v. *Gavit,* 268 U. S. 161. The income tax law provides that property acquired by bequest, devise or inheritance shall not be considered income, but that the income from such property shall be so considered. In *Irwin* v. *Gavit,* the income beneficiary of a testamentary trust sought to avoid income tax liability on the trust income distributed to him, asserting that such income was exempt under that provision. This Court overruled the contention, holding that the exempt bequest was the life interest in the estate, a capital asset which passed to the taxpayer from the decedent, and that the income arising therefrom after the decedent's death was not a part of such bequest but was a gain derived therefrom and therefore subject to income tax.

In *Koshland* v. *Helvering*, 298 U. S. 441, this Court held that income earned by a capital asset after any given date is not a part of the capital asset as of such date. Specifically, it was held in that case that a stock dividend which could have been taxed to the stockholder as income did not represent a portion of the stock originally acquired by him and, therefore, the Treasury had no right to require him to deduct the amount of such dividend from the cost of the original stock in order to determine his gain or loss upon a subsequent sale thereof. The Court said that "the Secretary of the Treasury is without power by regulatory amendment to add a provision that income derived from the capital asset shall be used to reduce cost". Of course, if the income did in fact represent a partial realization of the capital asset, as the Government contends in this case, it would be proper, even necessary, to reduce the original cost of the asset by the amount of such income.

Approval of the same general proposition is implicit in this Court's decision in *United States* v. *Safety Car Heating Company, supra.* It was held there that an amount received after March 1, 1913, on a claim for patent infringement which arose prior to that date did not constitute, in whole or in part, merely a partial realization of a capital asset owned on March 1, 1913, but was taxable in its entirety as income.

It is entirely clear that that which constitutes a part of a decedent's estate at the date of his death is subject to estate tax as having been transferred by reason of the decedent's death and is capital to those who receive it by bequest, devise or inheritance, and, therefore, is not taxable to them as income. *Cf. Lyeth*

v. *Hoey*, 305 U. S. 188. It is equally clear that the income earned by the estate after death is not a part of the estate, is not transferred by reason of the decedent's death and, therefore, is not subject to estate tax, but is a gain derived from the estate and taxable as income to those who receive it.

III.

Receipts after death may not be treated as if they were part of the decedent's estate, except to the extent that they deplete the original capital of the estate.

The very theory on which the Commissioner seeks to justify his Regulations—that the income represents a partial realization of the capital of the estate—demonstrates his error. If any income received by the executor during the one-year period constituted a partial disposition or realization of any asset held in the estate at the date of the decedent's death, the only procedure authorized by the statute, or even by the theory of the Regulation, would be to ascertain the portion of or interest in the asset so realized and include the same in the estate at its value at the time disposed of.

Any asset owned at the date of death which is "distributed by the executors * * * or sold, exchanged, or otherwise disposed of, shall be included at its value as of the time of such distribution, sale, exchange, or other disposition * * *, instead of its value as of the date one year after the decedent's death." In other words, if an asset owned at the date of death or any portion thereof or interest therein is disposed of within the one-year period, the proceeds received on

such disposition are not included in the valuation of the estate, but the asset or the portion thereof or interest therein thus disposed of is included at its value at the time of such disposition.

We have no desire to be technical. We concede that, as a practical matter, any amount derived from one of the original estate assets within the one-year period, which actually depletes that asset and in effect constitutes a partial realization or disposition thereof, might properly, to that extent, be included in the gross estate, in lieu of the portion of or interest in the original asset so realized or disposed of.

But the inclusion of any amount in the gross estate on any such theory would require a determination by the Commissioner that its receipt did actually exhaust or deplete the original capital asset to an ascertained extent.

In these cases the Commissioner has made no such determination. He merely has taken the position that any income earned by the estate after death must, as a matter of law, be considered to have exhausted or depleted the asset by which it was earned to the extent of its full amount and, therefore, must be taken into account in full.

The Commissioner's theory is patently erroneous. There are many kinds of income which might be earned by executors after the decedent's death which no one could with reason even claim to have any effect whatever on the original asset, by way of depletion or exhaustion.

For example, in the case of a patent or copyright, the executor may or may not put it to use during the one year after the decedent's death. If the executor

uses the patent or copyright, he may derive income from it, but it is perfectly clear that the fact that he has done so can have no effect whatever on its life or on its value except possibly to increase it. Whether or not the patent or copyright is used, it has a remaining life of one year less at the optional valuation date than it had at the date of the decedent's death and that diminution in its life may adversely affect its value, but such decrease in value would be caused "by mere lapse of time," and the statute expressly provides that changes in value due to "mere lapse of time" shall be disregarded.

Another example is a monopoly or franchise. It certainly cannot be contended seriously that the production of income from a franchise depletes or exhausts it or represents a partial realization or disposition of it. Here, again, if the franchise is for a limited period, there may be some decrease in value due to mere lapse of time. But no diminution in life or decrease in value can result from the production of income.

As a further example, take the case of a leasehold estate owned by the decedent at the time of his death. His executors may allow the property to remain unoccupied, or they may sublease it and thus derive income from it, but if they do that certainly will not shorten the leasehold or decrease its value in any way.

In the case of a franchise or other monopoly or lease which runs in perpetuity and not for a limited period of time, it is even more obvious that the productive use of such an asset during the year after death does not deplete or exhaust it or have any effect whatever on its value, except possibly to increase it.

The Treasury's theory is equally untenable with respect to income of any kind. It is inherent in the very concept of income from capital that it is a *gain* or *profit* derived from, and either severed or severable from, the capital, which leaves the capital undepleted and unimpaired.

Certain receipts, which in common practice often are treated as income, do to some extent deplete or impair the property from which they are produced. But, to the extent that they do so, they do not constitute true income but represent in part a return of capital and are not taxable as income.

For example, the owner of a mine is permitted to deduct from his gross receipts an appropriate amount to offset depletion; dividends paid out of a depletion reserve by a mining corporation are not considered taxable income. True stock dividends, representing merely a further division of the shares on which they are paid, and liquidating and other distributions out of corporate capital are not taxable income. The proceeds of the sale of an interest in property constitute income only to the extent they exceed an allocable portion of the cost of the entire asset.

As we shall show, the interest and dividends earned by the estates in the instant cases during the year after the decedent's death did not deplete or reduce the value of the bonds and stocks on which they were earned.

IV.

The interest and dividends earned after death, which the Commissioner has added to the estates herein, did not deplete the securities held in the estates or reduce the value thereof.

If interest received on a bond or a dividend received on stock represented a partial realization of the bond or stock itself, as contended by the Government, it readily can be seen that such interest or dividend would not constitute income in its entirety but that a portion thereof would represent a return of capital and only the excess would be subject to income tax.

The very fact that interest and ordinary dividends are taxable as income in their entirety is sufficient to demonstrate that they do not to any extent constitute a partial return of capital.

The Court of Appeals apparently recognized the impossibility of treating the same receipts as constituting at the same time both income and a return of capital. It solved the dilemma in *Maass* v. *Higgins* (No. 274), so far as it related to interest, by holding, in effect, that bond interest is not income in its entirety, and that although a portion of it is a realization of an increment in value of the capital investment, even that part is not ordinary income.

The court said that the value of a bond is the aggregate present value of all the obligor's promises to make payments in the future, including the promises to pay interest as well as the promise to pay principal, the value of each promise being discounted for the interval before its performance is due.

The court then said that although to the bondholder the interest payments "may appear to be the produce of his principal, it is not so", but that he gets, by way of principal and interest, more than he loaned "merely because a future dollar payable by another is less desirable than a present dollar in hand". The conclusion, of course, necessarily was that each payment, whether of so-called principal or of so-called interest, is merely a partial return of the original loan, increased in value because of the passage of time.

By this process of reasoning, the Court of Appeals (Judge Chase dissenting) held that the interest accrued and paid after death was but the realization of a part of the principal of the bond owned at death.

This Court has said that "the plain, obvious and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover". *Lynch* v. *Alworth-Stephens Company*, 267 U. S. 364, 370.

Nevertheless, if a quarter of a century ago it had occurred to any lawyer to advance the theory announced by the Court of Appeals, no one can say with certainty whether or not it would have been accepted by this Court. It can be said, however, with perfect assurance, that if such theory had been accepted by this Court, we should have had a far different income tax law from the one we have had, or have thought we have had.

Untold millions of bond interest on which income tax has been paid would have been free of income tax because it would have constituted a partial re-

turn of capital. Further millions received on the maturity of bonds, which have gone free of tax as a return of capital, would have been taxable as income. Moreover, the income resulting from the final payment of principal, and possibly even the income resulting from each payment of interest, would have been taxable at special rates as capital gain, rather than at full surtax rates as ordinary income (Int. Rev. Code, Sec. 117(f)).

The bench, the bar, the Treasury and the man in the street have assumed for a great many years that bond interest is ordinary income. Never before has it occurred to anyone to contend that it represents only a partial repayment of the principal of the bond, at an increased value.

The contention has been made, however, that if a bond is issued at a premium each payment of interest really represents, in part, not interest but a partial return to the purchaser *of the premium*. The contention was overruled by this Court, which said that "in the ordinary affairs of life no one stops for refined analysis of the nature of a premium or considers that the periodic payment universally called 'interest' is in part something wholly distinguished—that is, a return of borrowed capital". *Old Colony Railroad Co.* v. *Commissioner*, 284 U. S. 552.

If, as held by this Court in the *Old Colony Railroad* case, the receipt of interest does not deplete the premium at which a bond was issued, *a fortiori* it does not deplete the principal amount of the bond.

We submit it is far too late to recognize the revolutionary metamorphosis of the concept of bond interest attempted by the Treasury and the Court of Appeals by means of a new "interpretation" of gen-

eral language which has been on the statute books since 1916.

If the old rule, that bond interest is ordinary income and not to any extent a return of the original loan, be adhered to, it is clear that the receipt of interest when and as it accrues does not deplete or reduce the value of the principal obligation.

As to dividends, the majority of the Court of Appeals recognized some difficulty in applying to them the new theory which it had evolved as to bond interest. However, the court felt that Congress intended to treat all income during the year after death on the same basis and concluded that, since interest must be included in the gross estate, dividends must also be included, as well as rent from real estate.

The Court of Appeals overlooked the fact that this Court held, many years ago, that ordinary dividends paid in the usual course of business constituted, not a part of the stock itself, and not merely a realization of an increment in value of the stock, but ordinary income which neither depleted nor reduced the value of the stock and therefore were taxable as income in their entirety. *Lynch* v. *Hornby*, 247 U. S. 339. In that case it appeared that the dividends were paid out of earnings or profits accumulated by the corporation prior to 1913, but, nevertheless, it was held that since they were ordinary dividends paid in the usual course of business, they were income. The Court said, page 346:

> "We do not overlook the fact that every dividend distribution diminishes by just so much the assets of the corporation, and in a theoretical sense reduces the intrinsic value of the stock. But, at the same time, it demonstrates the

> capacity of the corporation to pay dividends, holds out a promise of further dividends in the future, and quite probably increases the market value of the shares. In our opinion Congress laid hold of dividends paid in the ordinary course as *de facto* income of the stockholders, without regard to the ultimate effect upon the corporation resulting from their payment."

This Court later pointed out that its decision in the *Hornby* case applied only to ordinary dividends paid in the usual course of business, and distinguished liquidating dividends and certain extraordinary dividends paid under special circumstances, which, because they depleted the stock to an equivalent extent, were considered merely a return of capital and not income. See *Southern Pacific Company* v. *Lowe*, 247 U. S. 330; *Lynch* v. *Turrish*, 247 U. S. 221; *Gulf Oil Corporation* v. *Lewellyn*, 248 U. S. 71.

It has been stipulated that all the dividends in the instant cases "were ordinary dividends and were not extraordinary or liquidating dividends, and were declared and paid or payable out of current earnings of the paying corporations or out of accumulated earnings of the paying corporations for years prior to the date of death" (R. 32, 51).

Exhibit A to the stipulation in the *Abendroth* case shows that, of the total dividends involved in that case, $623.25 consisted of fixed dividends on preferred stocks (R. 32-48).

Exhibit A to the stipulation in the *Blacque* case shows that, of the total amount of dividends involved in that case, $25,646.25 consisted of fixed dividends on preferred stocks (R. 62-83).

The stock dividends on which this Court ruled in the *Koshland* case consisted of a distribution of common shares on preferred shares. This Court held that such dividends were income which constitutionally might have been taxed by Congress and, therefore, although Congress had exempted all stock dividends from tax under the mistaken theory that they necessarily represented merely a return of capital, they "were income and may not be treated as a return of capital". A Treasury regulation which required that the stockholder's cost of his original stock should be reduced by the amount of such dividend was held to be unauthorized and invalid.

If dividends on preferred stock, payable in common stock, "may not be treated as returns of capital", *a fortiori* such dividends paid in cash may not be so treated.

The fact that the dividends received on the common stocks held by the two estates in these cases were ordinary dividends paid in the usual course of business appears not only from the express stipulation to that effect but also from the exhibits annexed to the stipulations.

The *Abendroth* estate held common or capital stock of *American Telephone and Telegraph Company*, on which the dividends which accrued during the year after death amounted to $9 per share, paid in four equal quarterly payments. It owned common class B stock of *American Tobacco Company*, on which the dividends amounted to $10 per share, in equal quarterly payments; 100 shares of *North American Company* common stock, on which one dividend of 50¢ per share and three dividends of 30¢ per share were paid; 50 shares of *Union Pacific Railroad* common stock,

on which four quarterly dividends of $1.50 per share were paid; 48 shares of common or capital stock of *Standard Oil Company of Indiana*, on which two quarterly dividends of 40¢ per share, one of 50¢ per share and one of $1.25 per share were paid (R. 34-35, 46).

The common stocks owned by the *Blacque* estate on which dividends were received during the year after death were: *American Can Company* which paid one dividend of $1 per share; *American Telephone and Telegraph Company*; *American Tobacco Company* class B; *Atlantic Refining Company*, which paid one dividend of 25¢; *Bigelow Sanford Carpet Company*, which paid only one dividend of 75¢; *Chesebrough Manufacturing Company*, which paid one dividend of $1.50; *Chrysler Corporation*, which paid one dividend of $2, one of $3 and one of $3.50; *Consolidated Edison Company*, which paid four quarterly dividends of 50¢; *Consolidated Oil Company*, which paid one dividend of 20¢; *Corn Products Refining Company*, which paid one dividend of 75¢; *Eastman Kodak Company*, which paid one dividend of $2; *General Cigar Company*, which paid one dividend of $1; *General Electric Company*, which paid one dividend of 30¢, two of 40¢ and one of $1; *General Foods Corporation*, which paid one dividend of 50¢; *General Motors Corporation*, which paid two dividends of $1; *International Business Machines Company*, which paid four quarterly dividends of $1.50; *International Nickel Company*, which paid three quarterly dividends of 50¢ and one of 75¢; *Lanston Monotype Machine Company*, which paid four quarterly dividends of $1; *Liggett & Myers Tobacco Company*, Class B, which paid four quarterly dividends of $1 and one extra dividend

of $2; *Monsanto Chemical Company*, which paid one dividend of 50¢; *National Biscuit Company*, which paid one dividend of 40¢; *Ohio Oil Company*, which paid one dividend of 50¢; *Pennsylvania Railroad*, which paid one dividend of 50¢ and one of 75¢; *Pullman, Inc.*, which paid one dividend of 37½¢; *Socony Vacuum Oil Company*, which paid two dividends of 25¢ and one of 30¢; *Standard Oil Company of California*, which paid one dividend of 35¢, two of 45¢ and one of 80¢; *Standard Oil Company of Indiana*, which paid one dividend of 25¢, one of 40¢, one of 50¢ and one of $1; *Standard Oil Company of Kentucky*, which paid one dividend of 40¢; *Standard Oil Company of New Jersey*, which paid two dividends of $1.25; *Texas Gulf Sulphur Company*, which paid one dividend of 75¢; *Union Carbide & Carbon Corporation*, which paid four dividends of 80¢; *Union Pacific Railroad*, which paid four dividends of $1.50; *United Fruit Company*, which paid one dividend of 75¢; and *Westinghouse Electric and Manufacturing Company*, which paid one dividend of $1 (R. 62-83).

In each instance the dividends earned on the stock during the year after death represented only a moderate rate of return on the value of the stock as included in the gross estate.

This Court held in *Helvering* v. *Gowran*, 302 U. S. 238, that a dividend paid in preferred shares on common stock, which might have been treated as income under the Constitution, was income and not a return of capital, despite the fact that Congress had not taxed it as income. It was held that the stockholder could not allocate a part of the cost of his original common stock to the preferred stock received as a dividend, but that when he later sold

such preferred stock the entire proceeds of the sale were taxable as income. It was held further that the dividend shares were separate and distinct from the original shares, not even in theory a part of them, and therefore could not be deemed to have been "held" by the taxpayer prior to the payment of the dividend for the purpose of determining the "holding period" for "capital gain" purposes. The Court said, page 244:

> "Whether taxed by Congress or not, it was income, substantially equivalent for income tax purposes to cash or property, and under §115(b) was presumed to have been made 'out of earnings or profits to the extent thereof, and from the most recently accumulated earnings or profits'. In no sense, therefore, can it be said to have been 'held' by Gowran prior to its declaration."

The Court held invalid certain regulations which proceeded on the theory that any stock dividend which Congress had not seen fit to tax as income constituted merely a part of the original stock on which it was paid. Of such regulation, the Court said, in a footnote on page 244 of its opinion:

> "But this was based upon the erroneous premise that stock dividends could not be income, and was part of an administrative scheme to apportion some of the cost of the original shares to the stock received by way of dividend. This arrangement we declared in *Koshland* v. *Helvering*, 298 U. S. 441, to be without statutory authority, and the same must be said of the Regulation involved here."

The dividend in the *Gowran* case was a dividend of $14 per share on common stock, payable in preferred

stock. It appeared that it was paid out of surplus earnings and that, apparently, was sufficient for this Court to hold that it was income to the stockholder. If a dividend such as that constitutes income and may not be treated as a return of capital or be deemed to have been "held" prior to its receipt, *a fortiori*, the dividends paid on the common stocks held by the estates in these cases must be viewed in the same light.

V.

The statute, being clear and unambiguous, requires no interpretation by Treasury regulation.

The Regulation can be sustained only if the statute is ambiguous and therefore requires interpretation. In *Koshland* v. *Helvering*, *supra*, this Court said, pages 446-447:

> "Where the act uses ambiguous terms, or is of doubtful construction, a clarifying regulation or one indicating the method of its application to specific cases not only is permissible but is to be given great weight by the courts. And the same principle governs where the statute merely expresses a general rule and invests the Secretary of the Treasury with authority to promulgate regulations appropriate to its enforcement. But where, as in this case, the provisions of the act are unambiguous, and its directions specific, there is no power to amend it by regulation."

As stated, this Court held in that case that stock dividends taxable as income (though not actually so taxed) are not a partial return of the original stock

investment, and that the Secretary of the Treasury had no power to treat them as such by regulation. See, also, *Helvering* v. *Gowran, supra.* Certainly, if stock dividends cannot be so treated, bond interest and ordinary cash dividends cannot.

The Treasury's feeling that the statute as enacted is unwise or contains some defect or omission, even if well founded, would not justify a correction of it by "interpretation".

There is, in fact, no defect or omission in the statute which needs correction. As has been shown, it would be a most unusual provision and would upset many fundamental principles of the law of taxation if the statute had provided for the inclusion in the decedent's estate of the income after death.

Of course, if the income after death had been required to be added to the estate, the relief which Congress admittedly desired to extend to estates would have been diminished, but there is no indication that Congress felt it was being too generous. On the contrary, as we shall show, there is positive proof in the legislative history of the provision that Congress intended to exclude the income after death.

VI.

The legislative history shows that Congress did not intend to subject income after death to the estate tax.

If, as the Treasury contends, the statute is ambiguous and requires interpretation, we are entitled to look to the legislative history for guidance.

Section 202 of the Revenue Bill of 1935, as sent to conference by the Senate and House, provided for amending Section 303(a) of the Revenue Act of 1926, allowing certain deductions in arriving at the net estate, so as to add a new section allowing a deduction for:

> "The net shrinkage in value of assets arising solely from the difference in the aggregate value of assets forming a part of the decedent's gross estate on the date of death and the aggregate value of such assets one year after the decedent's death * * *."

The deduction to be allowed was the difference between the value of the *assets* of the estate on the date of death and the value of *such assets* on the optional valuation date, signifying that the same assets should be valued on both dates and with no indication that any income accruing between those dates should be included in the valuation.

The purpose of the amendment was stated in the report of the Senate Finance Committee on the Revenue Bill of 1935 (74th Congress, First Session, S. R. No. 1240, pp. 9-10), as follows:

> "This provision is equitable in its effects and will prevent in practically all cases the danger of complete confiscation of estates due to a sudden decline in market values."

Section 202 was changed in conference to read as it was finally enacted, but its purpose remained unchanged. An explanation of that section and its operation is set forth in the report of the committee of conference on the Revenue Bill of 1935 (74th Congress, First Session, H. R. No. 1885, pp. 10-11).

The following illustration therein set forth is pertinent:

> "The operation of this new provision giving the executor an election may be shown by the following example:
>
> A decedent dies owning real estate of the value of $100,000, corporate stock of the value of $60,000, bonds of the value of $20,000, foreign government bonds maturing 9 months after date of death of a face value of $10,000, but of a value of $9,550, and cash amounting to $5,000. These values are as of the date of death. The gross estate at date of death amounted, therefore, to $194,550. The decedent had debts of $15,000 and the administration expenses were $25,000, which debts and expenses were promptly paid by the executor. The value of the net estate as of date of death was, therefore (after taking off the specific exemption), $114,550. Six months after the decedent's death the executor distributed the bonds to a legatee under the will, at which time they were worth $18,000, and he sold all the corporate stock owned by the decedent for a fair market value of $50,000 in order to raise cash to pay the debts and expenses. The foreign bonds were paid in full at maturity.[3] During the first year after the decedent's death the value of his real estate appreciated $5,000. The executor elects to take advantage of the new provisions of the bill. The value will be arrived at in this way:

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[3] The fact that these bonds were "paid in full" at maturity nine months after death shows that interest must have accrued *and been paid* on them after death. It is reasonable to suppose that the other assets also produced income after death.

Assets		Value
Real estate (as of 1 year after death)		$105,000
Corporate stock (as of date of sale)		50,000
Bonds (as of date of distribution)		18,000
Foreign bonds (as of date of disposition, *i. e.*, maturity)		10,000
Cash		5,000
Gross estate		$188,000
Deduct:		
Debts	$15,000	
Administration expenses	25,000	
Specific exemption	40,000	80,000
Net estate		$108,000"

The fact that the illustration does not show the inclusion of income accruing between the date of death and the optional valuation date (the only cash included is the $5,000 which the decedent had at the date of death) is a definite indication that Congress intended that such income should not be included.

VII.

The Treasury's contention, that its "interpretation" of the statute is necessary to prevent tax evasion, is unfounded.

The Treasury insists that the law must be interpreted to include in the estate the income after death, in order to prevent tax evasion. Several far-fetched, unlikely situations are referred to.

It is said that the executor may sell all the coupons from the estate's bonds, so that one year after death

the bonds will have lost a great part of their value, and that an unfair advantage would be obtained by the estate if the proceeds were not added to the estate in arriving at the value one year after death. The answer is obvious. Selling off coupons in advance of their maturity would materially alter the bonds; the mutilated bonds left in the estate would not be the same assets as the bonds owned at the date of death with all unmatured coupons attached. For example, they would not be good delivery against a contract to sell the original bonds. It seems clear that the original bonds would have to be valued at the date of such mutilation.

But clipping coupons and collecting the interest thereon *in regular course as they mature* does not alter the character of a bond; it remains what it always was, a bond with all unmatured coupons attached.

The answer is the same to the assertion that an estate could evade tax by commuting and collecting rent or royalties in advance.

The Treasury points also to large, extraordinary dividends paid within one year after death out of corporate surplus existing at the date of death as a possible means of tax dodging under the statute as written, especially where the decedent's estate owns a controlling interest in the corporation.

It cannot be denied that such extraordinary dividends might deplete and reduce the value of the stock owned at the date of death. To the extent that they do, we see no reason why such dividends should not be treated as effecting a partial disposition of the stock held at the date of death, thus requiring that

the full value of the stock before the payment of such dividends be included in the estate.[4]

However, it is not necessary to consider the question of such extraordinary dividends in these cases or in the companion case of *Maass* v. *Higgins*, in none of which are any such dividends involved.

It is sufficient here to point out that there is no basis, in logic or common fairness, for treating *ordinary dividends* paid in regular course of business (or *ordinary bond interest*) as constituting, at one and the same time, both capital owned at death and income earned after death, and thus subjecting them to the burden of double taxation.

Conclusion.

The Treasury's attempt to treat ordinary dividends and bond interest earned after death as constituting both income and a return of capital to the estate shocks common understanding, is unsound in theory, violates the fundamental distinction between capital and income, seeks to overthrow cardinal principles long established in the field of taxation, and ignores the plain language of the statute; all for the purpose of curing a supposed but really non-existent defect

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[4] In estate and trust accounting, extraordinary dividends are treated as principal to the extent they are paid out of earnings accumulated before death or before the creation of the trust, as the case may be. See *Matter of Osborne*, 209 N. Y. 450.

True stock dividends (a mere subdivision of shares) and liquidating and other distributions out of corporate capital present no problem. Such distributions are not income, but are treated as a partial return of capital under the tax law (Int. Rev. Code, Sec. 115(c), (d), (f)) and for all purposes.

in the law as enacted, by a method which would impose an unjust burden of double taxation which there is no reason to believe Congress would approve.

The decisions below are wrong and should be reversed.

Respectfully submitted,

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Appendix.

The Regulation.

Article 11, Regulations 80 (in part):

ART. 11. **Optional valuation date.**—In general, the object of subdivision (j) of section 302 is to make provision whereby the amount of tax otherwise payable may be lessened when, within the year following the decedent's death, the gross estate has suffered a shrinkage in its aggregate value.

If the decedent died after August 30, 1935, the executor may, by an election upon his return, Form 706, if filed within the time prescribed by law or prescribed by the Commissioner in pursuance of law, have the property which was included in the gross estate on the date of the decedent's death valued as of the applicable dates, as follows:

(1) Any property distributed, sold, exchanged, or otherwise disposed of within one year after the decedent's death, valued as of the date of such distribution, sale, exchange, or other disposition, whichever first occurs;

(2) Any property not distributed, sold, exchanged, or otherwise disposed of within such 1-year period, valued as of the date one year after the date of the decedent's death;

(3) Any property, interest, or estate which is affected by mere lapse of time, valued as of the date of decedent's death; except that an adjustment is to be made for any difference in its value, not due to such lapse of time, as of the date one year after the date of decedent's death, or as of the date of its distribution, sale, exchange, or other disposition, whichever date first occurs.

* * *

The property to be valued as of one year after the date of decedent's death, or as of date of decedent's

death, or as of some intermediate date, is the property included in the gross estate on the date of the decedent's death. As property and its value are separate and distinct, the former denoting legal rights, the latter the monetary measure of such rights, and as subdivision (j) treats of the two separately, it will be necessary in every case first to determine what property constituted the gross estate at decedent's death. Subdivisions of section 302, as amended, other than subdivision (j), supply the information necessary to that determination, subdivision (j) being, in the main, confined to the date or dates as at which the value is to be ascertained.

Interest-bearing obligations, such as bonds and notes, embody two promises, one to pay principal and the other to pay interest, and both promises are a part of the gross estate at the death of the decedent, if the obligation was then owned by him, or had been previously so transferred by him, or at his death there was vested in him any such right or power in or with respect to the obligation as to bring it within any of the other subdivisions of section 302, as amended. If the valuation date is that of decedent's death, the principal of the obligation and interest then accrued and unpaid thereon are to be valued as of that date. If the valuation date is subsequent to death, the principal and interest then accrued and unpaid are to be valued as of that date. The valuation date of any part payment of principal or of any installment of interest, made between decedent's death and the date as at which the obligation is to be valued, will be the date of such payment. Like rules will govern, so far as applicable, when any other obligation is involved, as, for example, one calling for the payment of rent or a royalty. Thus, in the case of rent, if the realty and the obligation to pay the rent reserved were parts of the gross estate at the time

of decedent's death, the value of the former must be determined as of the applicable valuation date, and also the value of the rent then accrued and unpaid reserved by the latter. The valuation date of any rent paid in the interim pursuant to the rental obligation will be the date of its payment.

As in the case of bonds and notes, the interest accrued and unpaid upon a judgment on the date as of which the judgment is to be valued is to be included in the valuation. The valuation date of any part payment of the judgment, or of any interest thereon (without regard to whether earned before or after decedent's death), made between decedent's death and the date as of which the judgment is to be valued, will be the date of such payment.

When corporate stock is a part of the gross estate at decedent's death, and a dividend in partial liquidation is thereafter paid on or before the date as of which the stock is to be valued, the valuation date of such dividend will be the date of its payment. Similarly, a dividend paid within the same period out of earnings, whether the earnings are made or accumulated prior or subsequent to decedent's death, will be valued as of the date of its payment. Earnings of the corporation neither declared as a dividend nor paid between decedent's death and the valuation date of the stock, will be reflected in the value of the stock. But a dividend declared prior to the valuation date of the stock and payable subsequent thereto will not be so reflected if the stock is selling "ex dividend" on such valuation date, but is to be valued as of that date.

Differing from payments of principal and interest in the case of bonds and notes, those made upon a judgment are not pursuant to a promise but to an obligation imposed by law, which obligation, in its totality, is a part of the gross estate at decedent's

death if coming within any of the other subdivisions of section 302, as amended. So, too, liquidating dividends and dividends paid from earnings are not pursuant to a promise but are referable to legal rights inherent in stock ownership.

By way of illustrating the operation of subdivision (j), there is given the following example in which the death of the decedent will be taken to have occurred December 1, 1935:

Description	Valuation date	Value at valuation date	Value at date of death
Improved real estate—not disposed of within year following decedent's death	Dec. 1, 1936	$30,000	$35,000
Rents accrued but unpaid under lease antedating decedent's death	Dec. 1, 1936	900	500
Rent paid Jan. 1, 1936	Jan. 1, 1936	600	.....
Bonds sold June 1, 1936	June 1, 1936	59,400	60,000
Interest accrued and unpaid thereon	June 1, 1936	400	400
Interest paid Apr. 1, 1936	Apr. 1, 1936	1,200	.....
Corporate stock—distributed to legatee Nov. 1, 1936	Nov. 1, 1936	100,000	200,000
Cash dividend paid upon such stock Aug. 1, 1936	Aug. 1, 1936	100,000	.....
Bonds matured and paid Oct. 1, 1936	Oct. 1, 1936	12,000	12,000
Interest accrued	.....	.....	80
Interest paid at maturity	Oct. 1, 1936	240	.....
Interest paid Apr. 1, 1936	Apr. 1, 1936	240	.....
Corporate stock—not disposed of within year following decedent's death, and upon which no dividend was paid in that period	Dec. 1, 1936	50,000	100,000
Total value of gross estate pursuant to the election	.....	354,980	.....
Total value of gross estate as of date of decedent's death	.....	.....	407,980

Properties, interests, or estates which are affected by mere lapse of time include patents, estates for the life of a person other than the decedent, remainders,

reversions, and other like properties, interests, or estates. The phrase "affected by mere lapse of time" has no reference to obligations for the payment of money, whether or not interest-bearing, the value of which changes with the passing of time. However, such an obligation, like any other property, may become affected by lapse of time when made the subject of a bequest or transfer which itself is creative of an interest or estate so affected.

* * * *

Deductions authorized under section 303 are limited to the extent that allowance thereof is not, in effect, given in the valuing of the gross estate. Property passing by decedent's will, or passing by a transfer made by the decedent in his lifetime (if the transfer was such as to require the property transferred to be included in the gross estate) to or for any such public, charitable, or religious uses as are described in section 303(a)(3) or in section 303(b)(3), is deductible at its value as of the date of the decedent's death, subject, however, to adjustment for any difference in value one year after such death, or at the date of the sale or exchange in the case of property sold or exchanged during such 1-year period. But no such adjustment may take into account any difference in value due to lapse of time or to the occurrence or non-occurrence of a contingency.

The election is available to the executor only at the time the return is filed, and only if the return is filed within 15 months from the decedent's death, or within the period of an extension of time for filing granted under the provisions of article 68 or 69 of these regulations. The election applies to all the property included in the gross estate on the date of the decedent's death. It can not be applied only to a portion of such property. The election, if exercised, can not be rescinded.